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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 268

NATURAL GAS PIPELINE COMPANY OF AMERICA
AND
TEXOMA NATURAL GAS COMPANY,
Petitioners,

vs.

FEDERAL POWER COMMISSION
AND
ILLINOIS COMMERCE COMMISSION,
Respondents.

CROSS-PETITION FOR THE WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The cross-petition of Natural Gas Pipeline Company of America and Texoma Natural Gas Company, hereinafter called "petitioners", respectfully shows:

A.

Summary Statement of the Matter Involved.

1. The respondent herein, Federal Power Commission, has filed in this Court a petition, Docket No. 265, for the writ of certiorari to the United States Circuit Court of Appeals for the Seventh Circuit to review a judgment of that Court entered on April 14, 1941.[1] Petitioners will file their brief in opposition to said petition in cause No. 265. By the present petition, petitioners seek review of certain questions, only in the event that this Court grants the petition in Docket No. 265.

2. This is the first rate regulatory proceeding under the Natural Gas Act (15 U. S. C. 717, *et seq.*, 52 Stat. 821, *et seq.*, effective June 21, 1938), hereinafter referred to as the "Act." The pertinent sections of the Act are set forth in the Appendix hereto, page 25. This proceeding was initiated by a complaint against petitioners filed with the Federal Power Commission, hereinafter called "Commission", by the Illinois Commerce Commission, hereinafter called "complainant" (R. Vol. I, p. 1). Involved in this proceeding is a so-called "interim" order (R. Vol. VIII, pp. 3942-46) entered by the Commission on July 23, 1940, directing petitioners on or before August 15, 1940, to file new schedules of rates and charges for natural gas sold at wholesale which should "reflect" a reduction in operating revenues of petitioner Natural Gas Pipeline Company of America of not less than $3,750,000 per annum (R. Vol. VIII, p. 3946). The order further provided that the new schedules "shall be effective as to all bills regularly rendered on and after September 1, 1940" (R. Vol.

1. Petitioners are not filing the record with this cross-petition, but intend that, to avoid duplication, the record filed in Docket No. 265 be used with this petition. Since petitioners have not been served with a copy of the record filed in cause No. 265, record references to the proceedings in the Court of Appeals are necessarily omitted in this cross-petition. However, it is assumed that the transcript of proceedings in the Court of Appeals, including the opinion and judgment, will be appended to Volume VIII of the record printed for use below.

VIII, p. 3946). The opinion of the Commission appears at R. Vol. VIII, pp. 3925-42. On August 8, 1940, the said Commission amended its order to extend the time for filing the new schedules to September 1, 1940.

3. Upon petitioners' petition for review under Section 19(b) of the Act (15 U. S. C. 717 r-b), the Circuit Court of Appeals for the Seventh Circuit set aside the so-called "interim" order as amended and remanded the case for further proceedings in conformity with its opinion. That Court held that the Commission erred:

a. in failing to include in the rate base and in the amount to be amortized an allowance as going-concern value of the actual costs incurred in developing the markets;

b. in fixing the period of amortization at twenty-three years, beginning with the commencement of petitioners' operations on January 1, 1932, several years prior to the enactment of the Natural Gas Act, and ending December 31, 1954, adopted by the Commission as the date at which the economic life of petitioners' reserves of natural gas would be exhausted, instead of the period beginning with the time when petitioners were first subjected to regulation by the enactment of the Natural Gas Act and ending December 31, 1954;

c. in failing to use the present fair value, including going-concern value, instead of the original cost of present facilities, in fixing the amount to be amortized; and

d. in failing to use present fair value, including going-concern value, of existing facilities other than gas reserves and the proper allowance under the principle of average investment for necessary future capital expenditures, in fixing the rate base, instead of reproduction cost undepreciated of present facilities and actual cost of future facilities only through the year 1942.

4. Petitioners, operated as a single enterprise (R. Vol. I, p. 11), are engaged in producing, purchasing, transport-

ing, and selling natural gas (R. Vol. I, p. 11). Petitioners built and now maintain and operate a pipeline from the Texas Panhandle, where the gas reserves are located, to a point near Joliet, Illinois (R. Vol. I, p. 514). With respect to sale, the Act applies only "to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use * * *" (Sec. 1, 15 U. S. C. 717). About 90% of the gas sold by petitioners is purchased in interstate commerce by Chicago District Pipeline Company for resale to public utilities in the Chicago area (R. Vol. I, p. 3); the remaining 10% is purchased in interstate commerce by public utilities for resale and by industrial consumers along the pipeline (R. Vol. I, p. 3). The rates at which petitioners sell at wholesale vary, dependent upon the use to which the gas is put by the ultimate consumer (R. Vol. II, p. 687-8). These rates or prices were fixed by private contracts at a time when petitioners constituted a strictly private enterprise, long prior to their being subjected to regulation by the enactment of the Natural Gas Act. Petitioners have not held, and do not now hold, themselves out to sell gas to all who apply, but have confined their sales to a few selected buyers under private contracts (R. Vol. I, p. 11). This case differs from the ordinary public utility case in that petitioners have not themselves dedicated their properties to a public use. Another distinction between this case and the ordinary public utility case is that petitioners are engaged in an extractive industry, the life of which is definitely limited to the life of the source of supply of natural gas.

5. The undisputed facts are: (1) petitioners' sales are private sales to a few selected buyers; (2) petitioners are not a common carrier; (3) they have not constituted themselves a public utility or dedicated their property to the public use by offering to sell their commodity to all who apply; and (4) the industry in which they are engaged is

not one in which "free competition had been 'degraded into anarchy'" (*Sunshine Anthracite Coal Co.* v. *Adkins*, 310 U. S. 381, 395) (on the contrary, respondents contend that petitioners are too prosperous). Despite these facts the Court of Appeals held that the Act as applied to petitioners is valid under the Fifth Amendment to the United States Constitution. That Court also held that the Act and the regulation sought to be imposed are valid under the Fifth Amendment despite the fact that the Act and such regulation operate to take the use of petitioners' property for the public interest, and prohibit petitioners from withdrawing their property from such use except by permission of the Commission. This ruling is probably in conflict with the decision of this Court in *Wolff* v. *Court of Industrial Relations*, 262 U. S. 522.

6. The Commission did not determine just and reasonable rates and fix the same by order as required by Section 5(a) of the Act (15 U. S. C. 717 d). The Commission merely required that new schedules be put in effect reflecting a reduction in operating revenues to the extent of $3,750,000 per annum (R. Vol. VIII, p. 3946). Petitioners sell gas at various prices for various types of uses (R. Vol. II, p. 687-8). There is no evidence in the record upon which the Commission can determine what the various charges and rates should be. In failing to determine just and reasonable rates and fix the same by order, the Commission failed to carry out the mandate of the statute. The Court of Appeals nevertheless held that this procedure "while irregular and unusual * * * was in no way harmful or prejudicial" to petitioners, and overruled petitioners' contention that for this reason the order is improper and invalid under the Natural Gas Act.

7. The Commission's finding that petitioners' present rates are unreasonable (R. Vol. VIII, p. 3945) is unsupported by any evidence. The Commission was concerned

not with petitioners' rates but only with petitioners' profits. It is apparent from the Commission's opinion and findings that the Commission sought to impose a barely nonconfiscatory return (R. Vol. VIII, p. 3925-46). A rate yielding a return "substantially higher" than a barely nonconfiscatory return may be reasonable (*Banton* v. *Belt Line Corp.*, 268 U. S. 413). Neither the Commission nor complainant introduced any evidence going to the reasonableness or unreasonableness of petitioners' present rates. *Petitioners sell at various rates; not one of these rates was considered by the Commission for the purpose of determining its reasonableness or unreasonableness.* The only fact in the record in any way bearing on the question of reasonableness of the existing rates is that petitioners now earn $2,966,852 a year in excess of the barely nonconfiscatory return and the annual amortization allowance allowed by the Commission. The Court of Appeals held that the rate base fixed by the Commission was inadequate, because it did not include an allowance for present fair value including going-concern value. That Court also held that the annual amortization allowance fixed by the Commission was inadequate because the Commission failed to use present fair value including going-concern value. The average annual earnings of petitioners for the first seven years of the enterprise have been $1,234,118 per year in excess of the amount allowed by the Commission for amortization and return (R. Vol. V, p. 3005). During the whole period from 1932 to 1954, inclusive, petitioner's average annual earnings will be only $1,598,262 per year in excess of the amount allowed by the Commission for amortization and return (R. Vol. V, p. 3023).

The record does not support the Commission's finding that this excess constitutes the rates unjust and unreasonable, but on the contrary shows that the excess is reasonable on account of the great risks and hazards involved in

petitioners' business, their past deficits, their declining future returns, and the creative skill and efficiency of the management in the conception, the designing, the construction, and the operation of the enterprise. With respect to petitioners' business, the Circuit Court of Appeals said:

> "They (petitioners) present an amazingly interesting picture of the difficulties of long distance transportation of natural gas, of the tremendous effort, skill, and risk taken by these companies, of the extraordinary improvements necessary in construction and other apparatus, of economic management of business—securing fill-in contracts in slack periods, and maintaining high loads in pipe lines, without which petitioners' business would be on the rocks (or invoking Sec. 77B of the Bankruptcy Act) instead of perplexing commissions and courts with questions arising out of large profits."

The Court of Appeals stated the problem with respect to lack of substantial evidence to support the Commission's finding that the present rates are unreasonable, but did not state any conclusion thereon.

8. The evidence upon which the Commission relied in fixing the rate of return at 6½% contradicts rather than supports the Commission's finding. There is no substantial evidence to support the finding. The figures adopted by the Commission in its opinion (R. Vol. VIII, p. 3939) show that the cost of capital to petitioners would be 6.72%. In addition to the cost of capital, petitioners must be allowed compensation to cover risk, creative enterprise, engineering skill, and especially skillful management. The Court of Appeals erroneously held that there was substantial evidence to support the finding of the Commission that 6½% is an adequate rate of return.

9. Despite the uncontradicted fact that the yield on securities, as nearly risk free as could be obtained, is not more than 2%, the Commission fixed the interest rate to be used in computing the annual allowance for amortiza-

tion by the sinking-fund method at 6½% (R. Vol. VIII, p. 3945), frankly stating in its opinion that it is fair to fix such interest rate at the same figure as the allowed rate of return (R. Vol. VIII, p. 3938). The Circuit Court of Appeals did not consider or pass on this point. That Court erred in failing to hold the action of the Commission on this point to be error.

The Commission overlooked the purpose of the sinking-fund method of computation. The purpose of the sinking fund is to insure a return of the amount to be amortized to the investor at the end of the amortization period. The Commission's order compels the petitioners to speculate to get a return of the amount to be amortized.

10. The Commission adopted the sinking-fund formula for amortization and, hence, purported to adopt an undepreciated rate base. With respect to the physical properties, the Commission did not deduct the observed depreciation from 1932, when petitioners commenced operations, to 1939, the date of the investigation; however, with respect to the gas reserves, the Commission took the value as of June 1, 1939, and thus deducted the depletion of the gas reserves. On the Commission's own theory, petitioners are entitled to a fair return on an undepreciated rate base, but the Commission's order does not permit a return on such a rate base. The finding of the Commission as to the rate base, so far as the Commission went, is based upon petitioners' evidence accepted by the Commission. On that evidence and on the Commission's theory, the Commission's order is on its face confiscatory. The Court of Appeals did not consider this point and thus erred in failing to hold that the Commission's order is confiscatory on this ground.

The Commission allowed the sum of $1,557,852 as the annual allowance for amortization computed by the sinking-fund method using as base a 23-year amortization pe-

riod, and 6½% compound interest on the s ..ud accruals (R. Vol. VIII, p. 3945). The Co' ..ixed the amount to be amortized at $78,284,009, w.. ..ne Court of Appeals held to be too low. The annual amortization allowance will not yield that figure on the basis fixed by the Commission. It will produce only $78,045,648. On the basis of its own figures as to the proper amount to be amortized, the Commission's mathematical error results in confiscation of $239,361. The court of Appeals erred in failing to hold that the Commission's order is confiscatory on this ground.

11. Petitioners were required to proceed with their evidence shortly after the beginning of the hearing before the Commission's Trial Examiner and before a case had been made against petitioners (R. Vol. I, p. 15-34). At the conclusion of petitioners' direct testimony (when only 7 of petitioners' 37 witnesses had been cross-examined), a motion by counsel for the Commission and complainant for an "interim" order was filed (R. Vol. VIII, p. 3903-14) and the Commission's so-called "interim" order was entered (R. Vol. VIII, p. 3925-46). The hearing before the Commission has not been concluded (R. Vol. VIII, p. 3946). Under Section 5(a) of the Act (15 U. S. C. 717 d) the Commission has authority to enter an order fixing rates only after a "hearing." The Court of Appeals erroneously held that the so-called "interim" order was within the Commission's jurisdiction and authority.

B.

Jurisdiction.

The jurisdiction of this Court is sustained by Sec. 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (43 Stat. 938, 28 U. S. C. 347 a) and is also sustained by Sec. 19(b) of the Act (15 U. S. C. 717 r-b). The judgment of the Court of Appeals was entered on April

14, 1941. No petition for rehearing was filed in that Court. The present petition is filed within three months of the entry of the judgment of the Court of Appeals.

C.

Questions Presented and Reasons for Allowance of the Writ.

1. Is the Act, insofar as it purports to authorize the regulation of petitioners' prices for natural gas sold in interstate commerce, fixed by contract prior to the enactment of the Natural Gas Act, invalid as applied to petitioners and petitioners' business because in violation of the Fifth Amendment to the Constitution of the United States?

In view of the facts set forth above in paragraphs 4 and 5, the holding of the Court of Appeals that the Fifth Amendment is not violated is probably in conflict with the decisions of this Court cited in the annexed brief in support of this petition (p. 20, *post*).

If the decision of the Court below is not so in conflict, it decided an important question of Federal law which has not been, but should be, settled by this Court. The question of the validity of the Act is of national importance and concern.

2. Are the Act and the regulation sought to be imposed thereunder invalid under the Fifth Amendment because their necessary operation would be to convert petitioners' property and business from a strictly private to a public use and prohibit petitioners from withdrawing from or discontinuing their business except by permission of the Commission?

The holding of the Court of Appeals that the Fifth Amendment is not violated in this regard is probably in conflict with the decisions of this Court in *Wolff* v. *Court of Industrial Relations*, 262 U. S. 522.

If the decision of the Court below is not so in conflict, it decided an important question of Federal law which has not been, but should be, settled by this Court.

3. Does Section 5(a) of the Act require the Commission, after a proper finding based on substantial evidence that the existing charges are unjust and unreasonable, to determine the just and reasonable rates in each classification of sales by petitioners and fix each new rate by order?

In holding that Section 5(a) of the Act does not require the determination and fixing of rates, and requires no more than consideration of profits, the Court below decided an important question of Federal law which has not been, but should be, settled by this Court. The importance of the question goes far beyond this particular case. The proper administrative procedure under the Act should be settled by this Court. Furthermore, the Court below so far sanctioned a departure from the accepted and usual course of administrative proceedings as to call for an exercise of this Court's power of supervision.

4. Is the Commission's finding that petitioners' present rates are unjust and unreasonable supported by substantial evidence?

The Commission's finding that 6½% per annum is an adequate rate of return is based solely on the Commission's conclusion that petitioners' profits are excessive because they are in excess of a barely compensatory return. That this conclusion is erroneous clearly appears from the holdings of the Court below, namely: that the rate base upon which the Commission measured profits is inadequate; that petitioners' business involves extraordinary risks and hazards; and that the earnings of petitioners have been substantially increased by creative skill in design and construction of their facilities, efficient management in the operation of these facilities, and in the developing and maintaining of an exceptionally high load factor. In the

light of these circumstances, the fact that the earnings or profits exceed a barely nonconfiscatory return will not sustain a finding that the charges producing such earnings are unjust and unreasonable. A basic question is whether Section 5(a) of the Act (15 U. S. C. 717 d) requires a finding upon the reasonableness of *each rate* presently charged by petitioners, or whether a general conclusion as to petitioners' profits is a sufficient basis for a finding that *each rate* of petitioners is unreasonable. This question of the proper construction of the Act should be settled by this Court. A proper finding on the issue of reasonableness of present rates is, under Section 5(a) of the Act, a jurisdictional prerequisite to the fixing of new rates. A determination of this question now is important in this case in order that justice be done between the parties, and that a continuation of the hearing, if unnecessary, be obviated. Further, such a determination is important as to what quantum of proof is necessary to support a finding that existing rates are unjust and unreasonable and as to the elements which must be considered in arriving at such a finding.

5. Is the Commission's finding that 6½% per annum is a fair rate of return for petitioners supported by substantial evidence?

In holding that this finding is supported by substantial evidence, the Court below has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision. The Court below ignored the evidence on which the Commission relied in its opinion, which evidence was to the effect that cost of capital to petitioners would be 6.72%. Furthermore, the Court below failed to give effect to the compelling and uncontradicted evidence on other factors entering into the fixing of a proper rate of return.

6. In computing the annual allowance for amortization by the sinking-fund method, did the Commission err in

disregarding the undisputed evidence as to the earnings which can be realized from investments in the nearest to risk-free securities and in using as the compound interest rate on the sinking-fund accruals the same rate as the rate of return allowed?

This novel and important question should be settled by this Court. A determination of this issue will be more far-reaching than this particular case. If there is to be a continuation of the hearing in this case, a guide to a correct decision should be given.

7. Is the Commission's order confiscatory on its own findings and conclusions in view of its deduction of depletion on the gas reserve in fixing the rate base and mathematical error in computing the annual allowance for amortization?

8. Does the Commission have jurisdiction and authority under the Act to require a respondent whose rates are challenged to present its evidence before a case is made against it, and to enter an "interim" order at the conclusion of such respondent's direct testimony?

9. Does the presentation of the respondent's direct testimony with only partial cross-examination in a proceeding before the Commission under the Act constitute a "hearing" within the meaning of the Act?

Questions 8 and 9 above are important procedural questions under the Act; their significance goes far beyond this particular case. In holding the so-called "interim" order in this case is valid, the Court below decided important Federal questions in a way probably in conflict with the applicable decisions of this Court cited in the annexed brief, page 24, *post*.

If the decision of the Court below is not so in conflict, it decided important questions of Federal law which have not been, but should be, settled by this Court.

Further, the Court below so far sanctioned a departure from the accepted and usual course of administrative proceedings as to call for an exercise of this Court's power of supervision.

Petitioners show to this Court that each of the questions above specified is an important question; that they are of especial significance under the Act; that if this Court reviews the issues raised in the petition for the writ of certiorari in cause No. 265, the questions herein specified should also be reviewed.

WHEREFORE, your petitioners pray that, if this Court grants the petition for the writ of certiorari in cause No. 265, this petition be granted and that the writ of certiorari issue to the Circuit Court of Appeals for the Seventh Circuit for the purpose of reviewing the questions hereinbefore specified; that the judgment of the Court of Appeals be modified to provide that the order of the Commission be vacated and set aside and the cause remanded to the Commission with directions to dismiss the proceedings; and that petitioners be granted such other and further relief as to this Honorable Court shall seem meet.

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BRIEF FOR PETITIONERS IN SUPPORT OF CROSS-PETITION FOR THE WRIT OF CERTIORARI.

OPINIONS BELOW.

The opinion of the Commission appears at R. Vol. VIII, pp. 3925-42, and is not officially reported.

The opinion of the Circuit Court of Appeals for the Seventh Circuit appears in Vol. VIII of the record, and is not yet officially reported.

JURISDICTION.

The grounds upon which the jurisdiction of this Court is invoked are stated in the foregoing petition (p. 9, *supra*).

STATEMENT OF THE CASE.

A determined effort is made to limit the following statement to those facts which, in addition to the facts stated in the petition, are essential to an understanding of the questions presented and the reasons assigned for the allowance of the writ.

1. **Origin of the Enterprise.** In 1926 it was known that the Texas Panhandle gas field contained enormous reserves of natural gas (R. Vol. I, p. 493). No prospective markets for this gas were available within the distance ordinarily traversed by natural gas pipe lines at that time; but in the Midwest, several large centers of population, including the Chicago area, were not served with natural gas (R. Vol. I, pp. 493-4). At that time some of those who afterwards became the owners of petitioners con-

ceived the idea of developing a pipe line system traversing the more than 950 miles from the gas field to the Chicago area. Great mechanical and economic difficulties were presented. There was no history by which to gauge the prospect of such an undertaking. Gas pipe lines then in operation traversed only short distances (R. Vol. I, p. 494), and utilized a thick-walled, lap-weld pipe held together at the joints by couplings (R. Vol. I, pp. 494-5). Gas was then transported from pressures ranging from 400 to 500 pounds per square inch (R. Vol. I, p. 497). The proposed line to Chicago traversed a territory crossed by 31 rivers. A problem which demanded solution was the solidification under pressure of the moisture contained in natural gas into hydrates which blocked the passage of the gas in the pipe line (R. Vol. I, pp. 507-8). Years of research and experimentation followed. By 1930 sufficient progress had been made to undertake the venture (R. Vol. I, p. 502). A thin-walled, seamless pipe and also a thin-walled, electric-welded pipe had been developed as a result of petitioners' efforts, each of which weighed substantially less per lineal unit than the old type of pipe, and each of which could be utilized in large diameters under operating pressures in excess of 700 pounds to the square inch (R. Vol. I, p. 506). Means for removing the moisture from natural gas and thus preventing the formation of hydrates had been developed by petitioners (R. Vol. II, p. 650).

2. **Petitioners' Properties.** Petitioners acquired large reserves of natural gas in the Texas Panhandle field. After culling and consolidating their holdings, petitioners now have leases on about 150,000 acres (R. Vol. I, p. 623). Petitioners have drilled or acquired 171 wells (R. Vol. I, p. 623). An ever-present hazard in the maintenance of these wells is the accumulation of salt in the formation or well which blocks off the gas (R. Vol. I, p. 455). The maintenance of the wells involves the treating for "salting", blowing

water out, etc. (R. Vol. I, pp. 627-8). During the remaining life of their gas supply petitioners will have to drill and equip about 215 additional wells to meet their market requirements (R. Vol. II, pp. 864, 882). In spite of petitioners' efforts to protect their gas reserves, only 40% of the gas withdrawn from under petitioners' leases has been produced through petitioners' wells, the other 60% having been lost through drainage to low-pressure areas in the field (R. Vol. I, p. 240). These are but some of the many factors which make for great uncertainty in petitioners' source of supply.

A gathering system, including mains 24" in diameter and smaller lateral lines, was constructed out over the gas field for the purpose of gathering the gas at the wells and transporting it to a central point near Fritch, Texas (R. Vol. I, p. 531; Vol. II, p. 910). At Fritch, petitioners constructed their initial main compressor station. Also located at Fritch is petitioners' dehydration plant (R. Vol. I, pp. 467-8).

From Fritch, petitioners constructed their main pipe line 24" in diameter across Oklahoma, Kansas, Nebraska, Iowa, and on to Joliet, Illinois (R. Vol. I, p. 518). A map showing the route appears at R. Vol. V, p. 2687. About every 80 miles along the pipe line is a compressor station (R. Vol. I, p. 533). There are 10 such stations (R. Vol. I, p. 533). An aerial photograph of the Fritch station appears at R. Vol. V, p. 2803.

The 31 river crossings present a special hazard (R. Vol. I, p. 515). Petitioners have constructed two types of river crossings: an overhead suspension bridge and a multiple line submerged crossing (R. Vol. I, p. 520). A picture of an overhead suspension bridge appears in the record at R. Vol. V, p. 2783. A picture of a typical submerged crossing appears at R. Vol. V, p. 2785. Among the rivers crossed are the Missouri and the Mississippi (R. Vol. I, p. 526). One of the greatest risks confronting petitioners

is line failures (R. Vol I, p. 604). In February, 1938, petitioners suffered a line failure which cost about $250,000 (R. Vol. I, p. 604). Any break in the line involves the tremendous hazard of explosion and fire (R. Vol. I, p. 605). Petitioners are handling a highly explosive material under terrific pressures.

The fact that petitioners' facilities are operated at substantially higher pressures and stresses than have heretofore been employed by the pipe line industry presents a serious element of uncertainty (R. Vol. III, p. 1568). As the record shows, it is a matter of common knowledge that as equipment is worked or stressed toward ultimate capacity and is continuously employed at a very high percentage of total capacity, there is a tendency to fatigue, and in the absence of experience as a guide there is the serious question as to how long petitioners' facilities will hold up under the excessive strain, regardless of how well they are maintained or how well they have held up down to the present time (R. Vol. III, p. 1456).

3. **Petitioners' Marketing Contracts.** Since beginning operations petitioners have made a total of 161 contracts—all by private negotiation (R. Vol. II, p. 685). Of these contracts 47 are still in effect (R. Vol. II, p. 685). Twenty cover a supply of natural gas to be resold for domestic consumption (R. Vol. II, p. 685). These 20 contracts are referred to as "firm" contracts (R. Vol. II, p. 685). Under them petitioners are obligated to deliver gas to the capacity of their pipe line (R. Vol. II, p. 685). Of the remaining 27, two cover the sale of gas at the wells (R. Vol. II, p. 685), and 25 are for the sale of gas for industrial use (R. Vol. II, pp. 685-6). The industrial contracts are "interruptible" contracts (R. Vol. II, p. 686). They provide for an interruption of service in the event that petitioners are unable to supply the gas after the obligations of the firm contracts are met (R. Vol. II, p. 687). The interruptible contracts are divided into classes, each class taking

precedence over the lower classes in the event that petitioners are unable to serve all (R. Vol. II, p. 687). The higher classes pay a higher rate (R. Vol. II, p. 687). The interruptible industrial contracts do not obligate purchasers to take a minimum amount of gas (R. Vol. II, p. 687). These contracts are in fact only an option to the purchasers to take gas from petitioners' pipe line (R. Vol. II, p. 689). The total income under petitioners' firm contracts will not support petitioners' operations (R. Vol. I, p. 581).

The development of markets by petitioners up to the total capacity of their pipe line was a tedious, long, and expensive process. Prospective consumers of natural gas were using other fuels—artificial gas, oil, coal, kerosene, or distillate. The change-over from any of these fuels to natural gas involved expense and inconvenience, and efforts to introduce natural gas met with stubborn sales resistance (R. Vol. II, p. 1277), to overcome which required great expenditure of time, effort, and money (R. Vol. II, p. 677). It was not until 1936, four years after operations began, that the demand equaled the original rated capacity of petitioners' pipe line. (R. Vol. II, p. 676; Vol. III, p. 1329).

SPECIFICATION OF ERRORS.

The errors intended to be urged are those specified in the petition under "Questions Presented and Reasons for Allowance of the Writ" (pp. 10 to 14, *supra*), the Court below having ruled adversely to petitioners, or failed to rule, upon the questions there stated.

SUMMARY OF ARGUMENT.

The argument follows the order of the questions stated in the petition (pp. 10 to 14, *supra*).

ARGUMENT.

1. Constitutionality of Price Regulation Under the Act.

It is apparent that the decision of the Court below on this question is probably in conflict with the applicable decisions of this Court in *Williams* v. *Standard Oil Co.*, 278 U. S. 235; *New State Ice Co.* v. *Liebmann*, 285 U. S. 262; *Tyson* v. *Banton*, 273 U. S. 418; *Wolff* v. *Court of Industrial Relations*, 262 U. S. 522; *Michigan Public Utilities Com.* v. *Duke*, 266 U. S. 570; *Producers* v. *Railroad Commission*, 251 U. S. 228. In the foregoing cases this Court has consistently held (1) that the Fifth and Fourteenth Amendments prohibit price fixing on private sales of a commodity, no matter how useful or desirable the commodity may be to the public; and (2) that the Fifth and Fourteenth Amendments prohibit the conversion of a private business into a public utility by legislative fiat.

The cases of *Munn* v. *Illinois*, 94 U. S. 113, and *Townsend* v. *Yeomans*, 301 U. S. 441, are distinguishable in that petitioners have not themselves dedicated their property to the public use, and held themselves out to serve all who apply.

The cases of *Nebbia* v. *New York*, 291 U. S. 502, *Sunshine Anthracite Coal Co.* v. *Adkins*, 310 U. S. 381, and similar cases, are not in point, as the Court below recognized, in that those cases "all involved * * * critical, economic conditions which demanded legislative solution, and such critical condition and urgent necessity of immediate control are here absent".

The case of *Olsen* v. *Nebraska*, ... *U. S.* ....., decided April 21, 1941, is not authority for price fixing on private sales of a commodity. The legislation there under consideration limited the maximum charges of employment

agencies and was directed against frauds and unscrupulous dealings.

There is no significance to the fact that public utilities are purchasers of petitioners' natural gas. The public utilities also necessarily purchase other articles and commodities—pipes, compressor equipment, automobiles, gasoline, pencils, paper, etc. The decision below opens the door for legislative control of prices of all commodities—lumber, pipes, iron, ore, steel, food, oil, leather, etc. The importance of the question here raised is patent.

2. **Constitutionality of the Act and the Regulation Imposed in View of the Taking of Petitioners' Property for the Public Use With No Opportunity to Petitioners to Withdraw Except by Permission of the Commission.** That the decision of the Court below on this question is probably in conflict with the decision of this Court in *Wolff* v. *Court of Industrial Relations*, 262 U. S. 522, is evident. In that case this Court struck down as violative of the Fourteenth Amendment a state statute providing, *inter alia*, for the fixing of wages in meat-packing plants, the employer being, under the terms of the statute, required to pay the wages fixed and the employee being forbidden to strike against the wages fixed. The statute there prohibited the employer to cease business save on permission of the state authority. This Court termed such privilege to withdraw "illusory." In the case at bar petitioners cannot, under the Act, discontinue any present service without permission of the Commission; and the Commission may require them to extend their facilities and render additional service from which they may not withdraw without permission (Sec. 7; 15 U. S. C. 717 f).

If it be thought that this issue is not involved in this case because petitioners have not attempted to withdraw, attention is called to two points: (1) the employer in the *Wolff Case* had not attempted to withdraw; and (2) in the

case at bar, Section 21 of the Act (15 U. S. C. 717 t) imposes a fine or imprisonment, or both, upon any party who willfully and knowingly violates the Act. A statute, the validity of which may be tested only by a violation thereof at the risk of penalties, is unconstitutional (*Oklahoma Operating Co.* v. *Love*, 252 U. S. 331).

3. **Commission's Failure to Fix Rates as Required by the Act.** The Commission did not consider or determine the various rates for the various types of uses of natural gas. It did not consider or determine what spreads there should be between the various rates. It did not consider or determine whether there should be different rates. There is no evidence in the record upon which such determinations could be made. The language of Section 5(a) of the Act (15 U. S. C. 717 d) is mandatory. The language is clear: "the Commission shall determine the just and reasonable rate * * * and shall fix the same by order * * *."

The importance of this question of the proper construction of the Act is manifest. The decision of the Court below is erroneous. The question should be settled by this Court.

4. **Lack of Substantial Evidence to Support the Commission's Finding That Petitioners' Present Rates Are Unreasonable.** This question is not one of fact. Petitioners do not ask this Court to weigh evidence or settle a dispute of fact. The facts are clear and uncontradicted. The question is one of law. It has two aspects: (1) Does Section 5(a) of the Act (15 U. S. C. 717 d) require an examination of and finding upon the reasonableness of *each rate* charged by a natural gas company, or is a general conclusion (unwarranted here) that the company's profits are too great a sufficient basis for a finding that *each rate* is unreasonable? This is an important question of the proper construction of the Act. This question has not been, but should be, settled by this Court. It should be noted that a proper

finding of unreasonableness of present rates is a jurisdictional prerequisite to the fixing of new rates. (2) Is the quantum of proof sufficient to satisfy the requirement of substantial evidence as to the unreasonableness of each present rate, or even as to alleged excess profits? There is no evidence in the record as to the reasonableness or unreasonableness of the various present rates of petitioners. The present rates are presumptively reasonable. *St. Joseph Gas Co.* v. *Barker*, 243 Fed. 206. With respect to petitioners' profits, the facts set out in paragraph 7 of the petition (p. 5, *supra*) show that the profits are not excessive or unreasonable, particularly in view of the sound holding by the Circuit Court of Appeals that the rate base, upon which the Commission purported to measure the profits, is inadequate.

5. **Rate of Return.** The holding of the Court below that the Commission's finding of 6½% as a fair rate of return for petitioners is supported by substantial evidence is erroneous. A review of this question does not involve a dispute of facts. It is a legal question as to the quantum of proof required. A bare outline of the problem is stated in paragraph 8 of the petition (p. 7, *supra*). The decision below calls for an exercise of the supervisory power of this Court.

6. **Interest Rate on Sinking Fund.** The question of whether the interest rate on a sinking fund for amortization should be the same as the rate of return is a novel and important question which has not been, but should be, settled by this Court. The Commission's determination that the interest rate should be the same as the rate of return is based upon faulty reasoning and upon a misapprehension of the underlying reason for applying the sinking-fund method of amortization. This Court should exercise its power of supervision.

7. **Validity of "Interim" Order.** The question of the validity of the so-called "interim" order is a novel and important question which has not been, but should be, decided by this Court. It is apparent that the decision of the Court below that the Commission has implied powers under the Act is probably in conflict with the applicable decisions of this Court in *Siler* v. *L. & N. Co.*, 213 U. S. 175, and *I. C. C.* v. *C. N. O. & T. P. R. Co.*, 167 U. S. 479.

It is respectfully submitted that, if this Court grants the petition for the writ of certiorari in cause No. 765, the prayer of the present cross-petition should be granted.

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APPENDIX.

PERTINENT SECTIONS OF THE NATURAL GAS ACT.
(15 U. S. C. 717.)

SECTION 1. (15 U. S. C. 717.) (a) As disclosed in reports of the Federal Trade Commission made pursuant to S. Res. 83 (Seventieth Congress, first session) and other reports made pursuant to the authority of Congress, it is hereby declared that the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest, and that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest.

(b) The provisions of this Act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

SECTION 4. (15 U. S. C. 717c.) (a) All rates and charges made, demanded, or received by any natural-gas company for or in connectiton with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes or service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this Act takes effect) and in such form

as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect: *Provided*, That the Commission shall not have authority to suspend the rate, charge, classification, or service for the sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at

the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

SECTION 5. (15 U. S. C. 717d.) (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however,* That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

SECTION 7. (15 U. S. C. 717f.) (a) Whenever the Commission, after notice and opportunity for hearing, finds such action necessary or desirable in the

public interest, it may by order direct a natural-gas company to extend or improve its transportation facilities, to establish physical connection of its transportation facilities with the facilities of, and sell natural gas to, any person or municipality engaged or legally authorized to engage in the local distribution of natural or artificial gas to the public, and for such purpose to extend its transportation facilities to communities immediately adjacent to such facilities or to territory served by such natural-gas company, if the Commission finds that no undue burden will be placed upon such natural-gas company thereby: *Provided,* That the Commission shall have no authority to compel the enlargement of transportation facilities for such purposes, or to compel such natural-gas company to establish physical connection or sell natural gas when to do so would impair its ability to render adequate service to its customers.

(b) No natural-gas company shall abandon all or any portion of its facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities, without the permission and approval of the Commission first had and obtained, after due hearing, and a finding by the Commission that the available supply of natural gas is depleted to the extent that the continuance of service is unwarranted, or that the present or future public convenience or necessity permit such abandonment.

(c) No natural-gas company shall undertake the construction or extension of any facilities for the transportation of natural gas to a market in which natural gas is already being served by another natural-gas company, or acquire or operate any such facilities or extensions thereof, or engage in transportation by means of any new or additional facilities, or sell natural gas in any such market, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require such new construction or operation of any such facilities or extensions thereof: *Provided, however,* That a natural-gas company already serving a market may enlarge or extend its facilities for the purpose of supplying increased market demands in the territory in which it operates. Whenever any natural-gas company shall make application for a certificate of convenience and necessity under the provisions of this subsection, the Commission shall set the matter for hearing and shall give such reasonable notice of the hear-

ing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission. In passing on applications for certificates of convenience and necessity, the Commission shall give due consideration to the applicant's ability to render and maintain adequate service at rates lower than those prevailing in the territory to be served, it being the intention of Congress that natural gas shall be sold in interstate commerce for resale for ultimate public consumption for domestic, commercial, industrial, or any other use at the lowest possible reasonable rate consistent with the maintenance of adequate service in the public interest.

SECTION 19. (15 U. S. C. 717r.) (a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this Act to which such person, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. Upon such application the Commission shall have power to grant or deny rehearing or to abrogate or modify its order without further hearing. Unless the Commission acts upon the application for rehearing within thirty days after it is filed, such application may be deemed to have been denied. No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon.

(b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be served upon any member of the Commission and thereupon the Commission shall certify and file with the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order in whole or in

part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the judicial Code, as amended (U. S. C., title 28, secs. 346 and 347).

(c) The filing of an application for rehearing under subsection (a) shall not, unless specifically ordered by the Commission, operate as a stay of the Commission's order. The commencement of proceedings under subsection (b) of this section shall not, unless specifically ordered by the court, operate as a stay of the Commission's order.

SECTION 20. (15 U. S. C. 717s.) (a) Whenever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this Act, or of any rule, regulation, or order thereunder, it may in its discretion bring an action in the proper district court of the United States, the District Court of the United States for the District of Columbia, or the United States courts of any Territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices and to enforce compliance with this Act or any rule, regulation, or order thereunder, and upon a proper showing a permanent or temporary injunction or decree or restraining order shall be granted

without bond. The Commission may transmit such evidence as may be available concerning such acts or practices or concerning apparent violations of the Federal antitrust laws to the Attorney General, who, in his discretion, may institute the necessary criminal proceedings.

(b) Upon application of the Commission the district courts of the United States, the District Court of the United States for the District of Columbia, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have jurisdiction to issue writs of mandamus commanding any person to comply with the provisions of this Act or any rule, regulation, or order of the Commission thereunder.

SECTION 21. (15 U. S. C. 717t.) (a) Any person who willfully and knowingly does or causes or suffers to be done any act, matter, or thing in this Act prohibited or declared to be unlawful, or who willfully and knowingly omits or fails to do any act, matter, or thing in this Act required to be done, or willfully and knowingly causes or suffers such omission or failure, shall, upon conviction thereof, be punished by a fine of not more than $5,000 or by imprisonment for not more than two years, or both.

(b) Any person who willfully and knowingly violates any rule, regulation, restriction, condition, or order made or imposed by the Commission under authority of this Act, shall, in addition to any other penalties provided by law, be punished upon conviction thereof by a fine of not exceeding $500 for each and every day during which such offense occurs.